



# REVIEW & ANALYSIS

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## OF THE PRESIDENT'S FY 2003 BUDGET

MAJORITY STAFF  
SENATE BUDGET COMMITTEE  
KENT CONRAD, CHAIRMAN

FEBRUARY 6, 2002

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# TABLE OF CONTENTS

Letter from the Chairman . . . . .	3
Introduction . . . . .	4
Budget Overview . . . . .	6
Tax Proposals . . . . .	8
Discretionary Proposals . . . . .	10
Mandatory Proposals . . . . .	19
Economic Overview . . . . .	23
Budget Process . . . . .	26
Summary Tables . . . . .	27

## GENERAL NOTES

All years referred to are fiscal years, unless otherwise noted.

In the case of tables, text, and charts, detail may not add to totals due to rounding.

An “(\*)” means less than \$500 billion, less than \$500,000, or less than one-half percent.

# FROM THE CHAIRMAN



February 6, 2002

Sadly, President Bush's fiscal year 2003 budget request represents one of the most dramatic deteriorations in the nation's fiscal outlook we have ever seen. Just a year ago, the Bush administration held up projections of a record \$5.6 trillion ten-year surplus as proof that we could afford a massive tax cut, while still protecting Social Security and Medicare, paying down all available federal debt, and providing for the country's needs.

What a difference a year makes. The ten-year tax cut wiped out our best hope to prepare for the coming retirement of the baby boom generation, put a squeeze on other priorities, and left the nation ill-prepared for emergencies, such as the war on terrorism and the economic downturn.

The Bush administration has acknowledged a remarkable drop of nearly \$5 trillion in the projected surplus and a return to deficits for at least the remainder of President Bush's term in office. In 2002 alone, the Bush budget plan would put us more than \$100 billion in deficit. Over the ten-year period, 2002-2011, the Bush plan would use \$2.2 trillion of Social Security and Medicare trust fund surpluses to pay for the tax cut and other government expenses.

The sudden reversal in our fiscal position is both striking and disturbing. Instead of paying down the public debt to \$1.6 trillion in 2007, as promised in last year's budget, the Bush plan would leave us with nearly \$3.4 trillion of publicly-held debt in that year. Further, the reduction in debt paydown would force the government to spend more than \$1 trillion in additional interest costs over the next decade.

While the President's 2003 budget correctly provides additional resources for defense and homeland security, it calls for significant cutbacks in crucial areas, such as highway construction and repair, job training, and environmental programs. Other important initiatives, such as providing a Medicare prescription drug benefit, are badly underfunded. But the Bush budget may be most notable for what is left out entirely. The plan fails to provide any resources for the strengthening of Social Security in preparation for the retirement of baby boomers.

We must work together to restore fiscal discipline to the budget without abandoning the priorities of the American people or passing on a tremendous debt burden to our children. Unfortunately, President Bush's budget request takes us in exactly the wrong direction.

Sincerely,



KENT CONRAD  
Chairman  
Senate Budget Committee

## INTRODUCTION

*"There's some weird economics going on in Washington."*

– George W. Bush

In his recent State of the Union speech the President said that the deficits in his budget would be "small and short-term." But in the budget that was submitted on February 4, deficits total \$2.2 *trillion* over the 2002 through 2011 period when the surpluses in the Social Security and Medicare Hospital Insurance trust funds are excluded. And far from being temporary, the deficits in the President's budget extend through every year of the 10-year budget window (the deficit excluding Social Security and Medicare is \$150 billion in 2012, long after President Bush will have left office). The only way the President can claim the deficits are small and temporary is to ignore the long-term liabilities, or debt, represented by the Social Security and Medicare surpluses and focus on the unified budget.

Under the President's proposals, the unified budget will have deficits through 2004 (\$106 billion this year, \$80 billion in 2003, and \$14 billion in 2004) and then will return to surpluses. In 2003 through 2012 there will be a cumulative surplus of just over \$1 trillion. But focusing on that unified surplus seems to signal acceptance of the fact that more than \$2 trillion of the payroll taxes paid to provide for future Social Security and Medicare benefits will instead have to be used to pay for tax cuts and spending on other programs. This ignores the fact that every penny of those payroll taxes are already committed to Social Security and Medicare.

President's 2003 Budget: Deficits and Surpluses													
(\$ billions)	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	02-11	03-12
Deficit/surplus	-106	-80	-14	61	86	104	113	142	181	178	231	665	1,002
Excluding Social Security	-262	-259	-208	-156	-142	-139	-143	-124	-99	-119	-75	-1,651	-1,464
Excluding Social Security And Medicare	-297	-298	-252	-204	-195	-194	-201	-184	-163	-186	-150	-2,174	-2,027

The fiscal outlook painted in the President's budget is a far cry from the situation just one year ago. Then, both the Congressional Budget Office (CBO) and the administration told us that unified surpluses would total \$5.6 trillion in fiscal years 2002 through 2011 if policies remained unchanged. Now, the administration estimates the unified surplus for 2002 through 2011 will be just over \$2 trillion if policies remain unchanged.

But the President is proposing to dig the hole even deeper. He is proposing policies that would reduce the surplus for 2002 through 2011 by an additional \$1.3 trillion. The single largest reduction – more than \$400 billion in 2002 through 2011 (the cost in 2003 through 2012 is \$591 billion) – would come from additional tax cuts proposed by the President.

*The surplus has declined by almost \$5 trillion in 12 months*

<b>The Constantly Shrinking Surplus: \$5 trillion in 12 months</b>	
(\$ billions)	2002-11
<b>Total OMB baseline surplus April, 2001</b> .....	<b>+5,637</b>
Changes .....	-3,627
<b>Total OMB baseline surplus, January 2002</b> .....	<b>+2,010</b>
President's Budget proposals .....	-1,344
<b>Total surplus in Bush Budget</b> .....	<b>+665</b>
<b>Total decline in surplus</b> .....	<b>-4,972</b>

According to the administration, enactment of the President's policies would leave a unified budget surplus of \$665 billion in 2002 through 2011. That represents a reduction in projected surpluses of nearly \$5 trillion in less than a year. And, after excluding the surpluses of the Social Security and Medicare trust funds, there would be a deficit of nearly \$2.2 trillion. That is, nearly \$2.2 trillion of Social Security and Medicare payroll taxes would go to pay for tax cuts and other program spending through 2011.

*The Bush budget uses \$2.2 trillion in trust fund surpluses to pay for tax cuts and other spending.*

<b>Bush Budget Uses Social Security and Medicare Trust Funds for Tax Cuts and Other Programs</b>	
	2002-11
Social Security trust funds .....	1,651
Medicare trust fund .....	523
<b>Total use of trust fund surpluses</b> .	<b>2,174</b>

Last year, the President's budget claimed that even after enactment of the President's tax cut there would be \$2 trillion available to pay off all of the debt that would be available for redemption and that by 2007 outstanding debt would be down to \$1.6 trillion. Now the administration estimates that debt will total \$3.4 trillion by the end of 2007. And, we will spend nearly \$1.2 trillion more on interest payments than CBO projected in its baseline just one year ago.

## BUDGET BASELINE

*When CBO reestimates the President's budget plan, the \$1 trillion surplus projected by OMB is likely to be much lower.*

Estimates in the budget begin with projections of the cost of continuing current tax and spending policies. These estimates are affected by the underlying forecast for the economy, as well as projections of program participation for Medicare, Social Security and other benefit programs.

The current law baseline surplus displayed in the President's budget comes to \$2.9 trillion over the next decade (2003-2012), compared to a projection of \$2.3 trillion issued by CBO last week. Neither set of estimates assume the enactment of new policies.

They differ in part, because CBO followed current budget conventions and included the \$20 billion spent in fiscal year 2002 for anti-terrorism emergency spending as part of the baseline of government programs that will continue in future years. The White House treated that \$20 billion as a one-time expense and omitted it from the baseline. This explains more than one-third (\$246 billion) of the \$669 billion difference. OMB's economic forecast is also more optimistic than CBO's, and its estimate of spending for the Medicare program is \$300 billion lower than CBO's over the next decade.

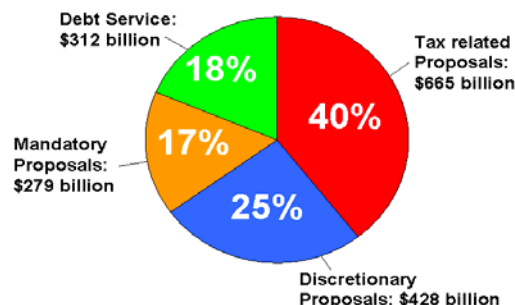
When CBO reestimates the President's budget, the surplus is likely to be much lower than the ten-year \$1 trillion surplus projected by OMB.

## BUDGET PROPOSALS

Proposals in the budget reduce baseline surpluses by \$1.7 trillion over the 2003-2012 period. A summary of these programs follows.

- Tax-related changes, including refundable tax credits, explain \$665 billion or 40 percent of the ten-year change.
- Discretionary spending programs increase by \$428 billion, or 25 percent, over the decade. Of this total, defense increases of \$595 billion are offset by nondefense cuts of \$167 billion.
- New mandatory spending for Medicare, the reauthorization of the farm bill, welfare reform, and other programs (except for the refundable portions of the tax credits which are counted with tax changes) totals \$279 billion over ten years, accounting for 17 percent of the changes.
- Higher debt service payments reduce the surplus by \$312 billion, or 18 percent.

**Proposals in the 2003 Bush Budget**



Proposals in the Bush Budget for Fiscal Year 2003			
(\$ billions)	2003	2003-07	2003-12
<b>Baseline deficits/surpluses (OMB-adjusted) . . . . .</b>	<b>+51</b>	<b>+764</b>	<b>+2,933</b>
Add back amounts for Sept. 11 emergencies . . . . .	-10	-95	-247
<b>Baseline deficits/surpluses (Normal conventions) . . . . .</b>	<b>+41</b>	<b>+669</b>	<b>+2,686</b>
Eliminate tax bill sunset . . . . .	-1	-22	-343
R & E tax credit . . . . .	-1	-14	-51
Tax stimulus . . . . .	-62	-87	-44
Incentives for charitable giving . . . . .	-2	-15	-40
Tax credits for the uninsured, long-term care, housing . . . . .	-(*)	-16	-65
Other tax extenders . . . . .	-3	-4	-4
Other revenue initiatives . . . . .	-4	-18	-44
<b>Subtotal, taxes . . . . .</b>	<b>-73</b>	<b>-176</b>	<b>-591</b>
<i>Taxes with refundables . . . . .</i>	<i>-74</i>	<i>-205</i>	<i>-665</i>
Defense . . . . .	-25	-197	-595
Homeland security and other nondefense . . . . .	+4	+60	+167
<b>Subtotal, discretionary . . . . .</b>	<b>-21</b>	<b>-137</b>	<b>-428</b>
Medicare and prescription drugs . . . . .	-2	-50	-190
Refundable tax credits . . . . .	-1	-29	-74
Farm bill reauthorization . . . . .	-7	-34	-68
Reform unemployment insurance . . . . .	0	-5	-22
Spending stimulus . . . . .	-8	-10	-10
Welfare reform . . . . .	-(*)	-2	-7
Spectrum auction . . . . .	-4	+7	+7
Medicaid drug pricing . . . . .	+(*)	+5	+18
Other mandatory . . . . .	-(*)	-2	-8
<b>Subtotal, mandatory . . . . .</b>	<b>-22</b>	<b>-120</b>	<b>-353</b>
<i>Mandatory without refundables . . . . .</i>	<i>-21</i>	<i>-92</i>	<i>-279</i>
Debt service . . . . .	-5	-78	-312
<b>TOTAL CHANGES . . . . .</b>	<b>-121</b>	<b>-512</b>	<b>-1,683</b>
<b>Deficit/Surplus (OMB) . . . . .</b>	<b>-80</b>	<b>+157</b>	<b>+1,002</b>

The President's budget includes proposals that reduce revenues by \$73 billion in 2003 and \$591 billion in 2003 through 2012. (Tax changes including refundable tax credits total \$665 billion over the ten years.) Tax reduction proposals include elimination of the tax bill sunset, permanent extension of an expiring research and development tax credit, an economic stimulus package, and a two-year extension of most expiring tax provisions. Specific initiatives include a new refundable tax credit to help parents of children in "failing public schools," as well as tax incentive proposals from last year on health insurance, long-term care insurance, and charitable contributions. The budget now calls for reform – not repeal – of the corporate alternative minimum tax (AMT), and only on a prospective basis.

**Elimination of tax bill sunset.** The President's budget proposes making permanent the tax changes enacted in 2001 that are scheduled to sunset in 2010. Eliminating the sunset would reduce revenues by \$343 billion over the period 2003-2012. However, the budget does not propose any changes in the increased exemption amount under the individual AMT which expires at the end of 2004, which would result in millions of taxpayers being added to the AMT rolls in the second half of the decade. (The budget acknowledges that 39 million taxpayers – 34 percent of all income taxpayers – will be affected by the AMT under the President's policies.) Nor does the budget appear to propose extending the deduction for college tuition that expires under current law in 2005.

Almost one-third of the costs associated with making the 2001 tax cuts permanent come as a result of eliminating the sunset of the estate tax repeal.

**Research and experimentation tax credit.** The President's budget would permanently extend the research and experimentation tax credit, which under current law does not expire until 2004, at a cost of \$51 billion.

**Economic stimulus (tax and spending).** The President's budget assumes the enactment of an economic stimulus and worker assistance package, but the tax incentives in the package are not focused on the short-term. It would provide \$89 billion in stimulus (including outlays) for 2002, but would cost \$122 billion in 2003 and 2004. An effective stimulus package should be heavily front-loaded to maximize its stimulative effect and minimize its contribution to outyear revenue losses. The budget also advocates accelerating upper-bracket tax rate reductions for individuals, which would bring tax relief to fewer than 30 percent of taxpayers. By definition these are the highest income taxpayers – those most likely to save rather than spend any additional cash. Accelerating the rate cuts is a permanent change to the tax code that will lose large amounts of revenue in 2003 and 2004, instead of concentrating its impact on 2002, where the need for stimulus is most acute.

**Incentives for charitable giving.** Between now and 2012, the President's budget proposes phasing in a charitable contribution deduction for non-itemizers that would cost about \$40 billion.



**Tax credits for the uninsured and long-term care insurance, and single-family housing.** The President's budget would provide refundable tax credits for the purchase of health insurance, long-term care insurance, and single-family housing. The tax piece alone reduces revenues by \$65 billion over ten-years. However, refundability may not make health insurance significantly more affordable for low-income individuals and families. The benefit of an above-the-line deduction for the purchase of long-term care insurance would accrue primarily to upper-income individuals who are already purchasing long-term care insurance on the individual market, especially in the near term since the level of the incentive would not become large enough to matter to most taxpayers until it reaches 100 percent in 2007. The proposed tax credit for developers of affordable single-family housing could fill a need in the affordable housing market. However, the proposed volume cap (\$1.75 per capita) may be insufficient, especially for low-population states.

**Extenders.** The President's budget proposes a \$4 billion two-year extension for tax provisions that expired in 2001 (retroactive to expiration date).

A summary table with additional tax detail can be found at the end of this report.

Discretionary spending includes those programs that are controlled through the annual appropriations process. About one-third of all federal spending is discretionary. Examples include funding for defense, highway construction, parks and wildlife, and government operations.

### OVERVIEW FOR 2003

For 2003, the President's budget includes substantial increases for defense and homeland security, a small increase for international affairs, and a *cut* of 6.2 percent for domestic programs (including transportation programs), relative to what is needed to maintain the same purchasing power provided to agencies and programs in 2002. Curiously, other than a proposal concerning Pell Grants, the Bush budget is silent about a supplemental appropriation for 2002, even though it is almost a virtual certainty that the administration will request additional resources this year for the war on terrorism and homeland security.

President Bush's budget requests \$766.9 billion in discretionary budget authority for 2003. Compared to an adjusted 2002 enacted level of \$717.8 billion,<sup>1</sup> the request represents an increase of 6.8 percent.

*Between 2002 and 2003, domestic programs (other than homeland security) are cut by 6.2 percent.*

However, when compared to OMB's estimate of the amount of resources needed to maintain the purchasing power provided to agencies and programs in 2002 – \$739.7 billion – the increase is 3.7 percent. All of the increase goes toward additional defense and homeland security funding. For domestic programs other than homeland security, the President is providing \$320.2 billion – a *cut* of 4.0 percent. When the Bush proposal for obligation limitations on discretionary transportation programs<sup>2</sup> (which for technical reasons are not scored as budget authority) is accounted for, the President's budget actually *cuts* funding for domestic programs other than homeland security by 6.2 percent.

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1. OMB estimates the enacted level for 2002 at \$709.3 billion, which includes the \$686 billion agreement, plus \$20 billion in supplemental emergency funds related to September 11 and \$3.3 billion in technical adjustments. Additionally, OMB has adjusted that number by \$8.5 billion to make it comparable with the President's request for 2003. That request includes additional amounts that will be required if Congress agrees to the President's proposal to adjust how the government accounts for the accrual cost of future pension and retiree health care benefits that its employees earn today and to convert three existing mandatory programs into discretionary programs. The \$8.5 billion adjustment represents the additional appropriations that would have been required if these proposals had been in effect in 2002.

2. The budgetary treatment of transportation spending is unique. For most transportation programs, the budget records budget authority as mandatory but outlays as discretionary. It is the annual appropriations process, however, that controls the level of new transportation spending through the use of obligation limitations. Thus, adding the amount of obligation limitations to the President's request for discretionary budget authority provides a more accurate picture of his proposal for new spending in appropriations bills.

**Comparing the Bush Budget for 2003 Discretionary Programs to OMB's Estimate of Amounts Needed to Maintain Purchasing Power at 2002 Levels**

Discretionary budget authority; \$ billions	OMB Baseline	Bush Budget	Budget Above/ Below Baseline	% Difference
Defense . . . . .	360.5	396.1	+35.6	+9.9%
International Affairs . . . . .	25.0	25.4	+0.4	+1.6%
Homeland Security . . . . .	20.5	25.2	+4.7	+22.9%
Other Domestic . . . . .	333.7	320.2	-13.5	-4.0%
Total Appropriations . . . . .	739.7	766.9	+27.2	3.7%
<b>Memorandum (with obligation limits):</b>				
Transportation . . . . .	37.9	28.4	-9.5	-25.1%
Adjusted Other Domestic . . . . .	371.6	348.6	-23.0	-6.2%
Adjusted Total Appropriations . . . . .	777.6	795.3	+17.7	+2.3%

## DEFENSE

The President's budget provides for the single largest increase in defense spending since 1982. For 2003, the budget provides a total of \$396.1 billion for defense, including \$379.3 billion for the Department of Defense. National Defense receives the single largest increase in any area of discretionary spending in 2003 and over the long term.

*The President's budget provides for the single largest increase in defense spending since 1982.*

President Bush announced a \$48 billion increase in budget authority for the Department of Defense over the 2002 level (but this includes changes in accrual accounting which lower the net additional funding available to the Department of Defense to \$45 billion). The increase includes a \$10 billion unallocated contingency fund for additional war expenses in 2003. The underlying budget request supports the war at the current tempo of operations.

Following in the footsteps of President Reagan during the Cold War, Bush's budget follows the large annual increase in 2003 with a long-term buildup. All told, Bush adds \$656 billion in national defense discretionary budget authority above the baseline level over the 10-year budget window.

Priorities for the 2003 budget are: continuing the war against terror, increasing investments in C4ISR (command, control, computers, communications, intelligence, surveillance, and reconnaissance) assets, converting four Trident ballistic missile submarines into cruise missile carriers, and accelerating F-22 fighter procurement from 13 jets per year to 23. The Navy's DD-21 destroyer is terminated, shipbuilding is cut from six vessels per year to five, low-priority military construction projects are delayed due to the delay in the base closure round to 2005, and 18 Army programs are terminated. Of the military services, the Air Force receives the largest increase (\$12.7 billion) and procurement gets the largest increase of the major accounts, rising \$7.6 billion to \$68.7 billion over the 2002 level.

President's Proposed \$48 billion Increase for the Department of Defense	
(Budget authority; \$ billion)	2003
2002 DoD Appropriation. ....	331
<u>Plus:</u>	
Inflation . . . . .	10
Contingency Fund. . . . .	10
Tricare for Life accrual. . . . .	2
Proposal to change accounting for pension and health accruals . . . . .	3
Other. . . . .	<u>23</u>
Total DoD adds . . . . .	48
2003 DoD Request. . . . .	379
<b>Memorandum:</b>	
Total Request for Defense Function, including \$17 billion for other defense activities 1/ . . . . .	396

1/ Among other things, includes funding provided to the Department of Energy for nuclear weapons and other defense- related activities

## INTERNATIONAL AFFAIRS

The Bush budget increases funding for international affairs from \$25.0 billion to \$25.4 billion, or by about 1.6 percent. (International programs received a total of \$24.2 billion for 2002.) That amount includes increases over the 2002 level of \$1.6 billion for development assistance (due in large measure to inclusion of funds for child survival and health) and \$310 million for diplomatic and consular programs. It also includes decreases of \$126 million for Support for Eastern European Democracy and \$27 million for peacekeeping operations. In addition, the President's budget proposal does not include additional aid to Afghanistan for 2003. It is possible such funds may be sought if the administration submits a supplemental request for 2002 later this year.

## HOMELAND SECURITY

*There is no agreed upon definition of homeland security.*

While the budget has included funding for homeland security for some time, September 11 has heightened the awareness of and need for such funding. Homeland security funding includes a variety of programs spread throughout the federal government. Because no agreed-upon definition of homeland security exists, disagreements may occur over the exact amount the federal government spends on these programs. For instance, for 2002, CBO estimates funding for nondefense homeland security at \$11.9 billion, while OMB estimates funding of \$19.8 billion.

For domestic homeland security programs, the President's 2003 budget provides \$25.2 billion. That amount is in addition to the \$12.5 billion he has included for homeland security under his defense request (for a total homeland security request of \$37.7 billion). In most cases, increases in homeland security

funding represent an increase in existing programs that the administration has identified as contributing to the mission of homeland security. The President's request of \$25.2 billion compares to a 2003 baseline level of \$20.5 billion, or an increase of 22.9 percent. The administration divides homeland security into four broad categories: supporting first responders (\$3.5 billion); defending against biological attacks (\$5.9 billion); border security (\$10.6 billion, including an additional \$406 million to the Coast Guard for port security); and sharing information and using technology (\$700 million).

In addition to funding for these programs, the budget includes \$4.8 billion for the newly-created Transportation Security Administration (TSA), which is responsible for coordinating and managing federal security efforts across all transportation modes. This represents a \$3.5 billion increase in aviation security funding over 2002. Over \$2.4 billion of this funding comes from expected receipts from the new \$2.50 per segment passenger security fee.

2003 Domestic Homeland Security Funding Request	
(\$ billions)	2003
Support for first responders . . . . .	3.5
Defending against biological terrorism . . . . .	5.0
Border security . . . . .	10.6
Sharing information and using information technology . . . .	0.6
Aviation security . . . . .	4.8
Other homeland security . . . . .	5.4
Passenger security and other fees . . . . .	-4.7
<b>Total . . . . .</b>	<b>25.2</b>

## OTHER DOMESTIC

The President's budget provides \$333.7 billion for 2003, \$13.5 billion below what is needed to provide agencies and programs with the same purchasing power as 2002. Because the budget provides some agencies and programs with levels above CBO's base for 2003, the cuts for other programs are greater than the average cut of 4.0 percent (6.2 percent when transportation spending authority is added). Below is a list of specific increases and cuts in the Bush budget.

## DISCRETIONARY INCREASES

**National Institutes of Health.** The President's budget contains a \$3.9 billion increase for the National Institutes of Health (NIH). This brings NIH's total budget to \$27.3 billion, completing the five-year program to double the agency's budget that began in 1998. However, over half of that increase, or \$2.3 billion, goes toward only two areas – bioterrorism and cancer. Bioterrorism research alone receives \$1.7 billion, while cancer research receives \$600 million.

**Other Discretionary Health.** For 2003, the President's budget requests \$63.7 billion in discretionary budget authority for the Department of Health and Human Services, an increase of \$2.7 billion, or 4.4 percent above the 2002 level. Increases in funding for the National Institutes of Health (NIH), which are included in this amount, equal \$3.9 billion. This means that \$1.2 billion of the NIH increase, as well as all other funding increases for discretionary health, are offset by cuts and freezes in other agencies and programs. These include the Centers for Disease Control and Prevention, the Human Resources and Services Administration, Ryan White AIDS Grants, maternal and child health, family planning, rural health initiatives, and mental health services.

**Education.** In total, the President's budget includes an increase of \$1.4 billion, or 2.8 percent, over the 2002 program level for Department of Education programs.

**Elementary and secondary education programs.** The budget includes a net cut of almost \$100 million for programs included in the "No Child Left Behind Act." To help pay for proposed increases of \$1.25 billion in specific programs, including \$1 billion for Title I grants for disadvantaged children, the budget cuts funding for other elementary and secondary education programs by nearly \$1.35 billion. It eliminates funding for 28 programs and other congressional priorities, including rural education, school counseling, drop out prevention, technology, teacher training, and school safety programs. It also cuts funding for Even Start, teaching history, and NAEP state tests.

By comparison, the budget includes a new refundable education tax credit for parents who transfer a child from a failing school to another public or private school. Under the proposal, a credit of as much as \$2,500 per year would be allowed for 50 percent of the first \$5,000 in tuition, fees, and transportation costs. The proposal's cost is estimated to be \$175 million in 2003 and \$3.7 billion over five years.

**Special Education.** For special education grants to states, the budget includes an increase of \$1 billion.

**Pell Grants.** Because more eligible students applied for Pell Grants over the past several years than had been projected, there is an estimated shortfall of \$1.3 billion in the program in 2002. To pay for a supplemental appropriation to meet this shortfall, the budget asks Congress to cut retroactively \$1.3 billion of enacted funding from a list of programs in the 2002 Labor, Health and Human Services, and Education appropriations bill.

For 2003, the President's budget freezes the maximum award at the current level of \$4,000. However, because more students are again expected to qualify for Pell Grants, the budget provides an increase of \$549 million over the 2002 appropriated level to accommodate the increasing number of eligible applicants.

**Safe and Stable Families.** The budget proposes \$200 million in discretionary funding for the Promoting Safe and Stable Families program, a \$130 million increase from the 2002 discretionary enacted level. This program provides family preservation services, family support, family reunification, and adoption promotion and support.

**Child Care & Development Block Grant (CCDBG).** The budget proposes to fund the discretionary piece of CCDBG at \$2 billion, a freeze at the 2002 enacted level.

**Women, Infants, and Children Program (WIC).** The budget proposes a \$364 million increase for WIC in order to serve 7.8 million people monthly who seek WIC services.

**Veterans.** The budget recommends a total of \$25.6 billion in discretionary funding for the Department of Veterans' Affairs. Of this amount, approximately \$23.5 billion is provided for medical care, an increase of \$1.4 billion over last year's level.

**Federal Emergency Management Agency (FEMA).** The President's budget creates a new program in the Federal Emergency Management Agency (FEMA) for emergency management planning and assistance. It includes \$3.7 billion for these activities. This increase is partially offset by the transfer of functions of the Office of Domestic Preparedness at the Department of Justice to FEMA as part of this initiative.

**Energy.** For the nondefense activities of the Department of Energy, the budget provides discretionary budget authority of \$21.8 billion for 2003, \$585 million (3 percent) more than the 2002 funding (figures adjusted to remove administration's accrual proposal).

**Agriculture.** The President's budget proposes to hold discretionary agricultural budget authority in 2003 at approximately \$19.4 billion, the same as the level in both 2001 and 2002.

## DISCRETIONARY CUTS

*Spending for highways is \$9.8 billion, or 30 percent, below last year's inflation adjusted level.*

**Highways.** The President's budget reflects a limit on highway program obligations in 2003 of \$22.6 billion. This represents a \$9.8 billion cut below the funding level needed to maintain last year's services, and a \$5.0 billion cut compared to the \$27.7 billion obligation limitation estimate for 2003 included in the Transportation Equity Act for the 21<sup>st</sup> Century (Public Law 105-178). Since the highway program spends out relatively slowly over time – approximately 27 percent in the first year – discretionary outlays for the total highway program will only drop by \$908 million in 2003 compared to 2002. Consequently, the Bush budget sets a new outlay cap for the highway program of \$27.581 billion in 2003 – \$908 million less than 2002. Each year, OMB adjusts the highway spending cap upward or downward to reflect changes in actual and projected receipts into the highway trust fund. The substantial cut in 2003 highway funding is largely due to lower than expected gas tax collections in 2001 and lower estimated gas tax receipts in 2003. The Bush budget provides no additional resources from the general fund to mitigate this sharp drop in funding for the highway program.

**Community Development Block Grant.** The President's 2003 budget cuts the Community Development Block Grant (CDBG) program by \$2.4 billion below the 2002 level to \$4.7 billion. When 2002 emergency funding is removed from the comparison, the cut is \$400 million. The CDBG program provides funding to local governments and communities to ensure decent affordable housing, and to provide essential services, create jobs and expand business opportunities.

*Environmental programs are reduced 8 percent below last year's inflation adjusted level.*

**Environmental.** The budget provides \$27.6 billion in discretionary budget authority for natural resources and environmental activities for 2003, which is \$1.4 billion, or 5 percent, below the 2002 enacted level.

- **Water Resources.** For 2003 water resources activities, the budget reduces the Army Corps of Engineers budget authority by \$599 million, or 13 percent, relative to its 2002 level. These cuts will slow completion of ongoing water infrastructure and ecosystem restoration projects in all 50 states, and prevent initiation of any new ones. In addition, the budget cuts funding for the Environmental Protection Agency's local wastewater and drinking water infrastructure activities by \$474 million, zeroing out funding for ongoing projects in at least 39 states.
- **Conservation Spending Category.** The budget fails to fully fund the Land, Conservation, Preservation and Infrastructure Improvement Fund (LCPPI), a conservation spending category established in 2001 to provide dedicated funding for programs addressing the loss of open space, wildlife habitat, wildlands and cultural treasures. LCPPI budget authority is authorized at \$1.92 billion for 2003, a \$160 million increase above 2002. Instead, the budget proposes to reduce funding to \$1.67 billion, 13 percent (\$251 million) below the authorized level, and 4 percent (\$66 million) below the \$1.74 billion 2002 enacted level.
- **Environmental Enforcement.** The budget reintroduces a 2002 proposal to divert Environmental Protection Agency (EPA) enforcement funds to states. This will reduce funds available for federal enforcement activities, and is estimated to result in a 162-person reduction in EPA federal enforcement staff.

**Job Training.** The President's budget cuts funding for discretionary employment and training programs by \$686 million below the 2002 enacted level. Although an additional \$73 million is requested for the Job Corps program, the budget cuts or eliminates funding for most other training programs. Specifically, it reduces Youth Opportunity Grants by \$181 million, or 80 percent, and assumes the program ends after 2003. It cuts youth activity grants by \$127 million, displaced worker assistance by \$166 million, and adult employment and training activities by \$50 million. In addition, the budget eliminates funding for the \$55 million Responsible Reintegration for Youth Offenders and the \$79 million Migrant and Seasonal Farmworkers programs.

**Agricultural Research.** The budget proposes reducing funding for agricultural research by \$574 million, or 14 percent, from the 2002 level.

**Community Oriented Policing Services.** The budget proposes to cut funding for the COPS program by \$469 million from the 2002 level, or by about 45 percent. Grant programs slated for reductions include: Public Safety and Community Policing Grants (-\$370 million), Crime Fighting Technologies (-\$69 million), and Community Crime Prevention (-\$23 million). Programs proposed to be eliminated include: the Law Enforcement Block Grant program (-\$400 million), the Boys and Girls Club of America (-\$70 million), the Cooperative Agreement Program (-\$20 million), the State Criminal Alien Assistance Program



(-\$565 million), and Byrne Grants (-\$594 million). Instead, the Administration proposes to create the Justice Assistance Grants program and funds it at \$800 million in 2003.

**Public Housing Assistance.** The budget proposes a \$417 million cut from the public housing capital building repair fund and the elimination of the \$25 million Rural Housing and Economic Development Fund.

**Low-Income Home Energy Assistance Program (LIHEAP).** The budget proposes \$1.7 billion for the LIHEAP program, \$1.4 billion in a regular appropriation and \$300 million in LIHEAP Contingent Emergency funds. The proposed level is a \$300 million cut from the 2002 enacted level.

**Centers for Disease Control.** The budget cuts funding for the Centers for Disease Control and Prevention by \$169 million, or 4 percent. Although the President allocates a substantial amount for bioterrorism preparedness at the agency, these monies are offset by deep cuts in other programs, including chronic disease prevention, infectious disease control, occupational safety and health, and public health improvement initiatives.

**Amtrak.** The President's budget provides \$521 million for Amtrak – a cut of \$100 million below the total 2002 funding level of \$621 million. The \$521 million funding level is \$679 million (57 percent) below the \$1.2 billion request that Amtrak recently announced it needs in order to preserve current services for all of its existing intercity routes. If funding is frozen at \$521 million, Amtrak has served notice that it may shut down most or all of its operations by the start of the 2003 fiscal year.

The following table lists the cuts made in the Bush budget from the 2002 level.

Agency or Program Cut	Changes from 2002	
	Dollars	Percent
Highways	-9.8	-30%
Community Development Block Grants	-2.3	-33%
Natural Resources and Environment	-1.4	-5%
Job Training	-0.7	-12%
Agricultural Research	-0.6	-14%
Community Oriented Policing Services	-0.5	-45%
Public Housing	-0.4	-15%
Low-Income Home Energy Assistance	-0.3	-15%
Centers for Disease Control	-0.2	-4%
Amtrak	-0.1	-16%

### 2002 SUPPLEMENTAL?

The most noteworthy omission in the President's budget request for discretionary programs may be its lack of a supplemental request,<sup>3</sup> even though the President is virtually certain to request one in the next few months. The Department of Defense is expecting additional 2002 funding to continue the war against terrorism. Additional funding for homeland security is also likely to be needed this year. By omitting the supplemental request from his budget, the President's budget has both a lower deficit estimate for 2002 and a smaller cut in domestic discretionary spending for 2003 (by understating the real funding level for 2002).

Comparing the Bush Budget for 2003 Discretionary Programs to 2002 Enacted Level, Adjusted for Proposal to Change Accruals				
Discretionary budget authority; \$ billions	2002 Enacted Level	Bush Budget	Budget Above/ Below Enacted	% Difference
Defense . . . . .	350.8	396.1	+45.3	+12.9%
International Affairs. . . . .	24.2	25.4	+1.2	+ 5%
Homeland Security . . . . .	19.8	25.2	+5.4	+ 27.3%
Other Domestic . . . . .	323.0	320.2	+2.8	+ 0.9%
<b>Total Appropriations . . . . .</b>	<b>717.8</b>	<b>766.9</b>	<b>+49.1</b>	<b>+6.8%</b>

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3. The budget does include a proposal to cancel \$1.3 billion in earmarked programs and projects included in the 2002 Labor-HHS appropriations bill and to provide an additional \$1.3 billion for Pell Grants in 2002.

Mandatory spending accounts for \$1.2 trillion or 55 percent of spending in the Bush budget in 2003 – a funding level equivalent to 10.6 percent of GDP. The largest mandatory programs in 2003 are Social Security (\$472 billion), Medicare (\$231 billion), and Medicaid (\$159 billion). Other mandatory programs, such as the earned income tax credit, food stamps, student loans, veterans' and other federal pension programs, account for \$297 billion in expenditures.

The President's budget proposes changes in mandatory spending that total \$22 billion in 2003, and \$353 billion over the next decade. The largest increases are for Medicare (\$190 billion), refundable tax credits (\$74 billion), and the farm bill reauthorization (\$68 billion). A Medicaid prescription drug pricing proposal assumes a spending reduction of \$18 billion and a shift in the spectrum auction deadlines saves another \$7 billion. Major changes in mandatory programs are described below. A summary table with additional detail on mandatory proposals can be found at the end of this report.

### SOCIAL SECURITY

The Bush budget raids the Social Security surplus in every year over the next ten years – for a total ten-year raid of \$1.6 trillion in 2002-2011. In addition, the Bush budget contains no resources to strengthen and preserve the Social Security program, even though the need for Social Security reform was highlighted in both the President's State of the Union speech and the President's 2003 budget documents. Actuarial analyses of the recommendations of the President's Commission demonstrate that significant budgetary resources will be needed in the current ten-year budget window to address Social Security reform, yet these resources are not accounted for or reserved in the President's current budget submission.

### MEDICARE

The President's budget for Medicare contains policy changes that increase mandatory spending on a net basis by \$1.7 billion in 2003 and by \$190.2 billion over the next decade (2003-2012). New initiatives include a low-income prescription drug benefit (\$77.1 billion), Medicare modernization (\$116 billion), payments to Medicare+Choice plans (\$3.7 billion), and the extension of premium assistance for low-income seniors (\$0.1 billion). These initiatives are partly offset by proposals that expand competitive bidding for durable medical equipment (-\$3.8 billion), create two new Medigap plans (-\$1.3 billion), require insurers to provide Medicare secondary payer data (-\$1.2 billion), and extend the GME update to hospitals with the highest per resident rates (-\$0.5 billion). The budget also proposed \$6.7 billion in reductions in Medicare administrative costs over the next ten years. These would be accomplished in part by a proposal to charge Medicare providers a \$1.50 processing fee on paper claims and a \$1.50 fee for sending in a duplicate claim or a claim with inaccurate or insufficient information.

In addition to legislative proposals to cut spending, the President intends to promulgate regulations that reduce Medicare spending. These policies include reductions in hospital disproportionate share payments, resource utilization group refinements for skilled nursing facilities, a modification of payments for covered outpatient prescription drugs, reforms of outpatient pass-through payments, and changes provider bad debt policies. These new regulations are

anticipated to reduce Medicare spending by more than \$30 billion over ten years. The President also intends to push ahead with a Medicare-endorsed discount card for seniors.

- The President's budget again proposes \$190 billion for Medicare reform and a prescription drug benefit (40 percent below the \$300 billion endorsed by Congress last year and the House leadership last week).
- The Bush proposal offers no new details on the kind of benefit the administration would design with \$190 billion. With respect to the President's Medigap plan, a similar option already exists but has failed to attract insurance companies or consumers. And the drug discount card – should it ever be put in place – saves much less than advertised. A recent GAO report found that the average discount offered on drug cards was less than ten percent, or \$3.31 per prescription – about what seniors could save by shopping among local pharmacies.
- The Office of Management and Budget (OMB) Medicare baseline is dramatically and mysteriously lower than it has been previously. With no written explanation, the OMB Medicare baseline dropped by \$196 billion from 2002 through 2011. Compared to CBO's January 2002 projections for 2003 through 2012, OMB assumes Medicare spending is \$300 billion – nearly 10 percent – lower. This baseline difference alone is equivalent to what Congress set aside last year to fund a prescription drug benefit.

*The Office of Management and Budget (OMB) Medicare baseline is dramatically and mysteriously lower than it has been previously.*

## OTHER MANDATORY

**Refundable tax credits.** The Bush budget proposes \$89 billion in refundable health tax credits intended to help families pay for health care coverage (see tax section above for more details).

**Farm bill reauthorization.** The Bush budget proposes \$74 billion in additional spending over the period 2002 through 2012 in order to fund reauthorization of the farm bill. Of the additional amount proposed, \$1.223 billion is to provide tax incentives for farmers and fisherman to establish savings accounts to supplement earnings in low-income years.

**Reform unemployment insurance.** The Bush budget proposes to cut the Federal Unemployment Tax Act (FUTA) payroll tax by 25 percent in 2003 and 75 percent by 2007 and thereby dramatically reducing federal payroll tax revenues supporting the federal unemployment system. The budget also proposes to allow states to use their own existing UI taxes to finance the cost of administering state UI and employment services programs (currently funded by the federal government with federal payroll tax revenues) and to provide billions of dollars from the federal Unemployment Trust Fund to states to help them finance their UI administrative operations in the short term.

**Welfare reform.** On a net basis, the Bush budget proposes to increase overall spending on welfare reform by \$9 million in 2003 and by \$6.5 billion over the period 2003-2012. Components of this proposal include:

- \$1 million for the reauthorization of the Temporary Assistance for Needy Families (TANF) supplemental grants in 2003 (\$319 million in budget authority) and \$45 million for a TANF contingency fund in 2003 (\$2 billion

in budget authority). The budget proposes a total of \$3.1 billion over the 2003-2012 period for these two programs. Separately, the Bush budget freezes the TANF block grant at \$16.7 billion for 2003;

- \$29 million increase for Food Stamps reauthorization in 2003; \$4.2 billion increase 2003-2012.
- \$66 million savings in Child Support enforcement in 2003; \$186 million increase 2003-2012
- \$903 million in SSI and Medicaid savings 2003-2012.

**Spectrum auction.** The Bush budget includes a proposal to shift the deadlines for two auctions of spectrum licenses, as well as ambiguous language about reforming the two auctions. The budget estimates that delaying those auctions by two years, from 2000 to 2004 and from 2002 to 2006, would increase federal receipts by \$6.7 billion over the 2003 - 2007 period. CBO, however, is expected to estimate savings from the proposal that are substantially less than the Administration's projection.

**Medicaid drug pricing proposal.** Under current law, manufacturers must pay states a minimum rebate per each unit of a drug dispensed equal to the higher of: 15.1 percent of average manufacturer price (AMP) or the difference between the AMP and the best price (the lowest price to most private purchasers). This proposal would increase the rebate significantly and save both the federal government and states money (the federal government shares in the rebate, because for every rebate dollar a state receives, the federal match is reduced accordingly). It would change the rebate to the higher of: 15.1 percent of average manufacturer price (AMP) or the difference between the average wholesale price (AWP) and the best price.

Because AWP is significantly higher (it is equivalent to a sticker price) than AMP (which is a truer price that manufacturers sell to most wholesalers), the spread becomes larger so the minimum rebate would increase. The budget assumes \$17.6 billion in savings over ten years for this proposal.

**ANWR.** The Bush budget assumes receipts of \$1.2 billion in 2004 from private sector payments for the right to drill for oil and gas in Alaska's Arctic National Wildlife Refuge. Drilling in this national wildlife refuge is currently not legal. Although the House has passed legislation to change current law, this proposal is highly controversial.

**Promoting Safe and Stable Families.** The Bush budget proposes \$305 million in mandatory spending for the Promoting Safe and Stable Families program in 2003, a freeze at the 2002 enacted level.

**Child Care Development Block Grant (CCDBG).** The Bush budget proposes \$2.7 billion in mandatory spending for CCDBG in 2003, a freeze at the 2002 enacted level.

**Social Services Block Grant (SSBG).** The Bush budget proposes \$1.7 billion in mandatory spending for SSBG in 2003, a freeze at the 2002 enacted level.

**Veterans.** The Bush budget proposes legislation to permanently extend IRS income verification on means-tested veterans' and survivors' benefits, which would allow savings of \$54 million over ten years.

The nation's longest economic expansion on record came to and end in March 2001. The unemployment rate, which had edged up from 4 percent in December 2000 to 4.3 percent in March, jumped to 5.8 percent by the end of the year.

## Unemployment Rate



## Recent Developments

The September 11 terrorist attacks dealt a severe blow to consumer and business confidence, and economic activity slowed sharply in the immediate aftermath of the attacks. However, economists' worst fears about the possible negative effects of the attacks were not realized, and recent data suggest that the contractionary phase of the current business cycle is coming to an end. Nevertheless, considerable uncertainty remains about when a sustainable recovery will begin and how strong an expansion we can expect.

The following are some key elements of that uncertainty:

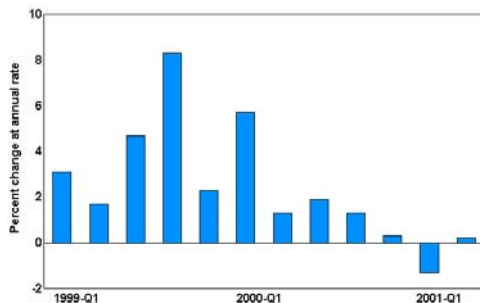
**Business investment.** This recession is unusual because it was precipitated by a sharp drop in business investment, particularly in business equipment and software. Very robust spending on such investment was a key driver in the late stages of the expansion, but investment appears to have raced ahead of demand, leaving substantial overcapacity to be worked off.

**Household spending.** This recession is also unusual because household spending has held up remarkably well. During the expansion, rising stock market wealth added to strong wage and income growth in fueling a consumption boom. Growth in household spending has slowed, to be sure, but it has remained strong enough—especially on housing and motor vehicles—to keep the decline in real GDP very mild so far. While this steadiness in consumption has been good for moderating the recession, it may also mean that there is less potential for a strong bounce-back in consumption as a source of strength in the recovery.

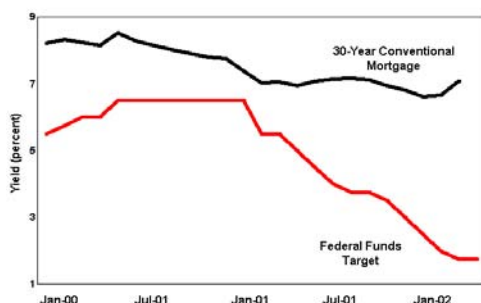
**Rest of the world.** Weak economic performance in the rest of the world means that the United States cannot count on robust demand for our exports as a source of strength in the recovery.

**Economic stimulus.** The fact that the worst of the contraction appears to be over reduces the need for economic stimulus as insurance against a disastrous collapse in economic activity. Moreover, the deterioration of the budget outlook appears to be one reason why long-term interest rates are about where they were a year ago despite aggressive reductions in short-term rates by the Federal Reserve. Policies offered in the name of stimulus can be a drag on the recovery if they substantially worsen the budget outlook.

## Real GDP



## Interest Rates



In contrast, policies that boost aggregate demand in the very near

*"...Over the past year, some of the firmness of long-term interest rates probably is the consequence of the fall of projected budget surpluses and the implied less-rapid paydowns of Treasury debt."*

*– Alan Greenspan  
Fed. Reserve Chairman  
January 11, 2002*

*"I do not think ...  
[economic stimulus] ...is  
a critically important  
issue to do. I think the  
economy will recover in  
any event."*

*– Alan Greenspan  
Fed. Reserve Chairman  
January 11, 2002*

term without seriously affecting the long-term budget outlook can strengthen the recovery in its early stages when a boost is most needed.

### **The Administration's Economic Outlook**

Like the Congressional Budget Office and the consensus of private forecasters, the administration is projecting an economic recovery this year. The administration explicitly predicates its assumptions on the adoption of the President's policies, including a stimulus package. CBO, by contrast, assumes no change in policy, while individual Blue Chip forecasters make their own assumptions about what policies will or will not be enacted.

Thus, very different policy assumptions underlie the fairly similar forecasts. In calendar year 2002, the Administration forecasts economic growth of 0.7 percent (compared with 0.8 percent for CBO and 1.0 percent for the Blue Chip consensus). For the 2002-12 period, all three predict that GDP will grow at an average annual rate of 3.1 percent. That CBO and the Blue Chip reach similar conclusions about growth in the short run without assuming adoption of the President's stimulus package is consistent with Fed Chairman Greenspan's view that economic stimulus is no longer critical to the recovery.

The Administration forecast in some ways seems designed to minimize deficits in the short run. For example, corporate profits before taxes are over \$100 billion higher in calendar year 2002 and \$74 billion higher in 2003 than they are in the CBO baseline. As a result, baseline revenues are higher in the early years in the administration forecast than they are in the CBO baseline.



Comparison of Economic Assumptions					
	Estimated	Forecast		Projected Annual Average Rate	
	2001*	2002*	2003*	2004-2007*	2008-2012*
Nominal GDP (year or end of period, \$ billions)					
OMB	10,197	10,481	11,073	13,614	17,404
CBO	10,193	10,422	11,063	13,639	17,532
Blue Chip	10,199	10,467	11,040	n.a.	n.a.
Real GDP (percentage change)					
OMB	1.0	0.7	3.8	3.4	3.1
CBO	1.0	0.8	4.1	3.3	3.1
Blue Chip	1.0	1.0	3.4	3.3	3.2
GDP price index (percentage change)					
OMB	2.3	2.0	1.8	1.8	1.9
CBO	2.2	1.4	2.0	2.0	2.0
Blue Chip	2.2	1.6	1.9	2.1	2.2
Consumer price index (percentage change)					
OMB	2.9	1.8	2.2	2.4	2.3
CBO	2.9	1.8	2.5	2.5	2.5
Blue Chip	2.9	1.7	2.4	2.7	2.6
Unemployment Rate (percent)					
OMB	4.8	5.9	5.5	5.0	4.9
CBO	4.8	6.1	5.9	5.2	5.2
Blue Chip	4.8	6.1	5.7	4.9	4.9
Three-month treasury bill rate (percent)					
OMB	3.4	2.2	3.5	4.2	4.3
CBO	3.4	2.2	4.5	4.9	4.9
Blue Chip	3.4	2.1	3.4	4.6	4.7
Ten-year treasury note rate (percent)					
OMB	5.0	5.1	5.1	5.2	5.3
CBO	5.0	5.0	5.5	5.8	5.8
Blue Chip	4.9	5.1	5.6	5.7	5.8
Sources: Office of Management and Budget; Congressional Budget Office; Blue Chip Economic Indicators, Aspen Publishers, Inc.					
Notes: January Blue Chip consensus for 2001-03; Blue Chip for 2004-2012 based on October 2001 long-run survey.					
* Calendar Years					

*The President does not propose new discretionary caps beyond 2002 or make assumptions regarding the extension of paygo enforcement provisions.*

Despite the fact that the discretionary spending caps and the main constraints of the pay-as-you-go (“paygo”) provisions of the Budget Enforcement Act expire on September 30, 2002, the President’s budget does not propose new caps beyond 2002 and makes no explicit assumptions regarding the extension of paygo (which requires that new mandatory spending and tax cuts be offset in order to avoid across-the-board cuts at the end of the fiscal year). Instead, the President’s budget states that the administration will work with Congress to develop budget enforcement mechanisms consistent with the needs of the country. If paygo and the discretionary caps are extended, the administration would support setting the caps at a level consistent with the levels of discretionary spending proposed in its budget, and paygo requirements that would carry out the mandatory spending and tax policies that it proposes. In addition, the President’s budget suggests several process reforms.

**Automatic continuing resolution.** The President’s budget proposes that if Congress and the President fail to complete action on all 13 appropriations bills by the October 1 start of each fiscal year, an automatic continuing resolution should go into effect to provide funding at the lower of the President’s budget or the prior year’s level.

**Joint budget resolution.** Currently, the budget that Congress considers each year is a concurrent resolution, meaning that it is considered by the House and Senate but is not subject to Presidential signature and does not become law. To give the budget resolution the force of law, the President’s budget advocates a joint budget resolution requiring the President’s signature and suggests that it could be enforced by sequesters requiring automatic across-the-board cuts by category to offset any excess spending.

**Line-item veto.** The Line Item Veto Act of 1996 attempted to give the President the authority to cancel spending and tax line-items, but the Supreme Court struck down that law as unconstitutional. The President’s budget proposes giving the President the authority to decline to spend new appropriations, to decline to approve new mandatory spending, or to decline to grant new tax benefits that are limited to 100 or fewer beneficiaries, whenever the President determines that the spending or tax items are not essential government functions and will not harm the national interest.

**Biennial budgeting.** The President’s budget envisions switching from the current annual budgeting and appropriating system to a two-year budget and appropriations process, whereby Congress would consider authorizing bills one year and appropriations bills the next.

**Advance appropriations.** The President’s budget aims to end the practice of advance appropriating, whereby funds appropriated do not become available until a year or more beyond the year for which the appropriations act is passed. It would cap 2003 advance appropriations at the amount advanced in the previous year, with certain programmatic exceptions.

# SUMMARY TABLES

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## FROM THE PRESIDENT'S BUDGET

- 1. Budget Authority Totals by Function**
- 2. Outlay Totals by Function**
- 3. Mandatory Proposals**
- 4. Effect of Proposals on Receipts**

**Table S-12. Budget Authority Totals by Function**  
(In billions of dollars)

Function	2001 Actual	Estimates					
		2002	2003	2004	2005	2006	2007
National defense.....	329.0	350.7	396.8	405.6	426.6	447.7	469.8
International affairs.....	18.7	22.3	23.9	24.8	25.6	26.3	27.2
General science, space, and technology.....	21.1	22.2	22.7	23.3	23.8	24.4	25.0
Energy.....	0.2	0.6	0.5	0.4	0.9	0.7	0.7
Natural resources and environment.....	29.8	30.9	30.0	31.3	32.3	31.7	32.3
Agriculture.....	29.2	29.0	23.8	23.0	21.3	20.4	20.3
Commerce and housing credit.....	12.4	10.7	14.1	9.8	9.4	8.5	10.7
On-budget.....	(8.4)	(7.8)	(8.9)	(9.4)	(8.9)	(8.1)	(9.5)
Off-budget.....	(4.1)	(2.8)	(5.2)	(0.4)	(0.5)	(0.4)	(1.2)
Transportation.....	67.6	66.1	63.7	58.4	64.6	65.9	67.2
Community and regional development.....	13.9	18.5	14.7	15.4	15.5	15.9	16.2
Education, training, employment, and social services.....	63.7	79.6	80.9	81.8	84.0	85.9	87.9
Health.....	182.1	201.0	234.3	259.0	278.4	298.0	319.9
Medicare.....	217.2	230.3	234.5	244.1	261.4	282.0	305.5
Income security.....	273.4	306.2	319.3	326.6	336.3	347.5	356.7
Social Security.....	440.5	461.3	476.9	497.6	521.8	548.5	577.8
On-budget.....	(11.7)	(13.9)	(14.3)	(15.2)	(16.1)	(16.9)	(18.0)
Off-budget.....	(428.8)	(447.4)	(462.6)	(482.5)	(505.8)	(531.6)	(559.8)
Veterans benefits and services.....	48.4	51.8	56.6	58.8	60.9	63.1	65.2
Administration of justice.....	45.0	37.3	38.2	41.0	38.9	39.8	40.7
General government.....	16.6	17.7	17.8	19.5	18.7	19.2	19.4
Net interest.....	206.2	178.4	180.7	188.8	190.2	188.3	185.3
On-budget.....	(275.0)	(255.2)	(264.5)	(280.9)	(291.2)	(299.3)	(307.4)
Off-budget.....	(-68.8)	(-76.8)	(-83.8)	(-92.0)	(-101.0)	(-111.0)	(-122.1)
Allowances.....	—	25.7	7.6	1.1	-0.4	-0.4	-0.4
Undistributed offsetting receipts.....	-55.2	-55.2	-74.1	-100.2	-100.4	-98.6	-98.4
On-budget.....	(-47.3)	(-45.9)	(-64.6)	(-89.9)	(-89.4)	(-86.8)	(-86.0)
Off-budget.....	(-7.9)	(-9.2)	(-9.6)	(-10.2)	(-11.0)	(-11.7)	(-12.4)
<b>Total.....</b>	<b>1,959.7</b>	<b>2,085.0</b>	<b>2,162.9</b>	<b>2,210.2</b>	<b>2,309.7</b>	<b>2,414.7</b>	<b>2,529.0</b>
On-budget.....	(1,603.6)	(1,720.9)	(1,788.5)	(1,829.6)	(1,915.5)	(2,005.4)	(2,102.6)
Off-budget.....	(356.2)	(364.2)	(374.4)	(380.6)	(394.2)	(409.3)	(426.4)

**Table S-13. Outlay Totals by Function**

(In billions of dollars)

Function	2001 Actual	Estimates					
		2002	2003	2004	2005	2006	2007
National defense .....	308.5	348.0	379.0	393.8	413.5	428.5	442.5
International affairs .....	16.6	23.5	22.5	22.8	23.3	23.9	24.6
General science, space, and technology .....	19.9	21.8	22.2	22.8	23.5	24.0	24.6
Energy .....	0.1	0.6	0.6	0.3	0.8	0.7	0.7
Natural resources and environment .....	26.3	30.2	30.6	31.1	31.7	32.4	32.8
Agriculture .....	26.6	28.8	24.2	22.8	21.3	20.4	20.3
Commerce and housing credit .....	6.0	3.8	3.7	5.1	3.1	1.2	1.7
On-budget .....	(3.7)	(1.7)	(5.1)	(4.4)	(3.3)	(2.1)	(2.5)
Off-budget .....	(2.3)	(2.0)	(-1.4)	(0.7)	(-0.2)	(-0.9)	(-0.8)
Transportation .....	55.2	62.1	59.4	56.3	56.0	56.9	58.6
Community and regional development .....	12.0	15.4	17.4	18.0	17.4	15.6	15.4
Education, training, employment, and social services .....	57.3	71.7	79.0	81.0	82.7	84.2	86.1
Health .....	172.6	195.2	231.9	258.8	277.8	297.0	318.3
Medicare .....	217.5	226.4	234.4	244.3	261.3	281.8	305.8
Income security .....	269.8	310.7	319.7	325.0	334.3	345.2	352.7
Social Security .....	433.1	459.7	475.9	495.7	519.7	546.2	575.3
On-budget .....	(11.7)	(13.9)	(14.3)	(15.2)	(16.1)	(16.9)	(18.0)
Off-budget .....	(421.4)	(445.7)	(461.6)	(480.5)	(503.6)	(529.3)	(557.3)
Veterans benefits and services .....	45.8	51.5	56.6	58.6	63.2	62.9	62.3
Administration of justice .....	30.4	34.4	40.6	43.5	39.5	39.7	40.4
General government .....	15.2	18.3	17.6	19.6	18.6	19.0	19.2
Net interest .....	206.2	178.4	180.7	188.8	190.2	188.3	185.3
On-budget .....	(275.0)	(255.2)	(264.5)	(280.9)	(291.2)	(299.3)	(307.4)
Off-budget .....	(-68.8)	(-76.8)	(-83.8)	(-92.0)	(-101.0)	(-111.0)	(-122.1)
Allowances .....	—	27.0	6.4	0.8	-0.5	-0.3	-0.4
Undistributed offsetting receipts .....	-55.2	-55.2	-74.1	-100.2	-100.4	-98.6	-98.4
On-budget .....	(-47.3)	(-45.9)	(-64.6)	(-89.9)	(-89.4)	(-86.8)	(-86.0)
Off-budget .....	(-7.9)	(-9.2)	(-9.6)	(-10.2)	(-11.0)	(-11.7)	(-12.4)
<b>Total .....</b>	<b>1,863.9</b>	<b>2,052.3</b>	<b>2,128.2</b>	<b>2,189.1</b>	<b>2,276.9</b>	<b>2,369.1</b>	<b>2,467.7</b>
On-budget .....	(1,516.9)	(1,690.6)	(1,761.5)	(1,810.1)	(1,885.5)	(1,963.4)	(2,045.8)
Off-budget .....	(347.0)	(361.7)	(366.8)	(379.0)	(391.4)	(405.7)	(421.9)

**Table S-9. Mandatory Proposals**

(In millions of dollars)

	2002	2003	2004	2005	2006	2007	Total	
							2003-2007	2003-2012
<b>Strengthening Medicare .....</b>	—	1,680	3,375	5,068	17,485	22,497	50,105	190,159
<b>Farm Bill <sup>1</sup> .....</b>	4,200	7,271	7,019	6,688	6,727	6,774	34,479	67,576
<b>Bipartisan Economic Security Plan <sup>2</sup> .....</b>	27,000	8,000	1,500	—	—	—	9,500	9,500
<b>Medicaid/SCHIP:</b>								
Medicaid/SCHIP reform .....	—	348	125	309	144	161	1,087	1,781
Rationalizing prescription drug payments .....	—	-290	-650	-1,090	-1,620	-1,800	-5,450	-17,640
<b>Welfare reform:</b>								
TANF reauthorization .....	—	46	314	270	340	387	1,358	3,069
Food Stamps reauthorization .....	—	29	148	262	329	355	1,123	4,191
Child support enforcement:								
Federal collections and payments to States .....	—	-66	-53	60	116	119	176	798
Food Stamps savings .....	—	—	—	-37	-47	-49	-133	-402
Medicaid savings .....	—	—	—	-5	-15	-20	-40	-210
Subtotal, child support enforcement .....	—	-66	-53	18	54	50	3	186
Supplemental Security Income .....	—	—	-2	-7	-13	-19	-41	-262
Medicaid savings .....	—	—	-3	-11	-25	-43	-82	-641
Subtotal, SSI .....	—	—	-5	-18	-38	-62	-123	-903
Subtotal, excluding Food Stamps reauthorization .....	—	-20	256	270	356	375	1,238	2,352
Total, welfare reform .....	—	9	404	532	685	730	2,361	6,543
<b>Other Proposals:</b>								
Agriculture:								
Increase timber competition (use of sealed bids) .....	—	—	-5	-10	-14	-15	-44	-139
Non-timber interests bidding .....	—	—	-5	-5	-10	-10	-30	-80
Collect fair market value from ski resorts .....	—	—	-3	-10	-14	-15	-42	-117
Accelerate repayment to reforestation trust fund and payments from special use permits to enhance environmental protection for lands used by ski resorts..	—	—	13	25	38	40	116	336
Provide permanent recreation fee authority .....	—	—	—	-10	1	1	-8	-3

**Table S-9. Mandatory Proposals—Continued**  
(In millions of dollars)

	2002	2003	2004	2005	2006	2007	Total	
							2003-2007	2003-2012
Education:								
Teacher loan forgiveness .....	—	45	14	17	18	18	112	211
Energy:								
Power marketing associations to directly fund Corps of Engineers' operations and maintenance expenses .....	—	149	149	150	150	150	748	1,498
Increase BPA's borrowing authority .....	—	—	113	498	89	—	700	700
ANWR, lease bonuses .....	—	—	-1,200	—	—	—	-1,200	-1,200
Health and Human Services:								
Abstinence education .....	—	14	37	42	47	50	190	440
Interior:								
ANWR, lease bonuses:								
State of Alaska's share:								
Receipts .....	—	—	-1,201	-1	-101	-1	-1,304	-1,587
Expenditure .....	—	—	1,201	1	101	1	1,304	1,587
Federal share .....	—	—	-1	-1	-101	-1	-104	-387
Provide permanent recreation fee authority .....	—	—	—	-17	7	48	38	490
Correct trust accounting deficiencies in individual Indian money investments .....	—	7	—	—	—	—	7	7
Labor:								
Reform Unemployment Insurance .....	—	—	—	319	1,929	3,072	5,320	21,812
Refinance Black Lung Disability Trust Fund debt:								
Black Lung Disability Trust Fund .....	—	1,606	-446	-435	-430	-427	-132	-2,184
Treasury's interest receipts .....	—	-1,606	446	435	430	427	132	2,184
Propose reforms of FECA for future beneficiaries .....	—	-3	-4	-6	-5	-5	-23	-46
Redirect H-1B training .....	—	80	-15	-48	-17	—	—	—
Treasury:								
Outlay effect of refundable tax credits .....	—	832	5,634	6,991	7,535	7,654	28,646	74,300

**Table S-9. Mandatory Proposals—Continued**

(In millions of dollars)

	2002	2003	2004	2005	2006	2007	Total	
							2003-2007	2003-2012
Veterans Affairs:								
IRS income verification on means tested veterans and survivors benefits .....	—	—	-6	-6	-6	-6	-24	-54
Army Corps of Engineers:								
Recreation user fee increase .....	—	-6	-1	-1	-1	4	-5	15
FCC:								
Shift spectrum auction deadlines:								
Spectrum receipts .....	—	4,000	-3,300	-2,700	-4,700	—	-6,700	-6,700
Spectrum relocation .....	—	50	-50	—	—	—	—	—
Impose annual analog fees after 2006 .....	—	—	—	—	—	-500	-500	-2,680
FEMA: Reform National Flood Insurance .....	—	-43	-75	-115	-165	-227	-625	-2,080
OPM:								
Simplify computation of annuities under the CSRS for individuals with part-time service .....	—	3	8	14	20	27	72	313
Multi-Agency:								
Authorize spending of reimbursements for spectrum relocating costs .....	—	100	50	100	165	100	515	715
Indirect impact of other proposals (third scorecard):								
Enact FECA surcharge .....	—	—	-1	-5	-7	-7	-20	-50
Impact of accrual accounting .....	—	-34	-23	198	420	618	1,179	7,686
<b>Total, mandatory proposals .....</b>	<b>31,200</b>	<b>22,213</b>	<b>13,102</b>	<b>16,927</b>	<b>28,800</b>	<b>39,358</b>	<b>120,400</b>	<b>352,906</b>

<sup>1</sup> Excludes Food Stamps reauthorization of \$4,191 million over 10 years shown under the welfare reform and the receipt effect of FFARRM account tax incentives of \$1,233 million over 10 years shown in Table S-10.

<sup>2</sup> Affects both receipts and outlays. Only the outlay effect is shown here. The receipt effect is -\$62,000 million for 2002, -\$65,000 million for 2003, -\$47,000 million for 2004, -\$9,500 million for 2005, \$17,000 million for 2006, \$18,000 million for 2007, -\$87,000 million for 2003-2007, and -\$43,500 million for 2003-2012.



**S-10. Effect of Proposals on Receipts**

(In millions of dollars)

	2002	2003	2004	2005	2006	2007	Total	
							2003-2007	2003-2012
<b>Bipartisan Economic Security Plan <sup>1</sup></b> .....	-62,000	-65,000	-47,500	-9,500	17,000	18,000	-87,000	-43,500
<b>Tax Incentives:</b>								
<b>Provide incentives for charitable giving:</b>								
Provide charitable contribution deduction for nonitemizers	-570	-1,429	-1,437	-2,288	-3,567	-3,591	-12,312	-32,636
Permit tax-free withdrawals from IRAs for charitable contributions .....	-93	-192	-205	-219	-230	-238	-1,084	-2,632
Raise the cap on corporate charitable contributions .....	-24	-169	-121	-127	-139	-156	-712	-1,730
Expand and increase the enhanced charitable deduction for contributions of food inventory .....	-10	-49	-54	-59	-66	-72	-300	-789
Reform excise tax based on investment income of private foundations .....	-122	-177	-181	-189	-198	-205	-950	-2,101
Modify tax on unrelated business taxable income of charitable remainder trusts .....	-1	-3	-3	-4	-4	-4	-18	-48
Modify basis adjustment to stock of S corporations contributing appreciated property .....	-8	-11	-13	-17	-21	-25	-87	-282
Allow expedited consideration of applications for exempt status <sup>2</sup> .....	—	—	—	—	—	—	—	—
<b>Strengthen and reform education:</b>								
Provide refundable tax credit for certain costs of attending a different school for pupils assigned to failing public schools <sup>3</sup> .....	—	-10	-24	-38	-52	-62	-186	-219
Allow teachers to deduct out-of-pocket classroom expenses .....	—	—	-16	-163	-191	-207	-577	-1,718
<b>Invest in health care:</b>								
Provide refundable tax credit for the purchase of health insurance <sup>4</sup> .....	—	-245	-1,689	-2,811	-2,774	-2,951	-10,470	-29,116
Provide an above-the-line deduction for long-term care insurance premiums .....	—	-328	-406	-605	-1,222	-2,158	-4,719	-20,730

# S-10. Effect of Proposals on Receipts—Continued

(In millions of dollars)

	2002	2003	2004	2005	2006	2007	Total	
							2003–2007	2003–2012
Allow up to \$500 in unused benefits in a health flexible spending arrangement to be carried forward to the next year.....	—	—	–441	–723	–782	–830	–2,776	–7,819
Provide additional choice with regard to unused benefits in a health flexible spending arrangement.....	—	—	–23	–39	–45	–52	–159	–566
Permanently extend and reform Archer MSAs.....	—	—	–43	–468	–530	–607	–1,648	–5,691
Provide an additional personal exemption to home caretakers of family members.....	—	–314	–383	–362	–345	–348	–1,752	–3,957
<b>Assist Americans with disabilities:</b>								
Exclude from income the value of employer-provided computers, software and peripherals.....	—	—	–2	–6	–6	–6	–20	–52
<b>Help farmers and fishermen manage economic downturns:</b>								
Establish FFARRM savings accounts.....	—	—	–133	–350	–244	–171	–898	–1,233
<b>Increase housing opportunities:</b>								
Provide tax credit for developers of affordable single-family housing.....	—	–7	–76	–302	–715	–1,252	–2,352	–15,257
<b>Encourage saving:</b>								
Establish Individual Development Accounts (IDAs).....	—	–124	–267	–319	–300	–255	–1,265	–1,722
<b>Protect the environment:</b>								
Permanently extend expensing of brownfields remediation costs.....	—	—	–193	–306	–299	–289	–1,087	–2,390
Exclude 50 percent of gains from the sale of property for conservation purposes.....	—	–2	–44	–90	–94	–98	–328	–918
<b>Increase energy production and promote energy conservation:</b>								
Extend and modify tax credit for producing electricity from certain sources.....	–92	–227	–303	–212	–143	–146	–1,031	–1,779

## S-10. Effect of Proposals on Receipts—Continued

(In millions of dollars)

	2002	2003	2004	2005	2006	2007	Total	
							2003–2007	2003–2012
Provide tax credit for residential solar energy systems ....	–3	–6	–7	–8	–17	–24	–62	–72
Modify treatment of nuclear decommissioning funds.....	–89	–156	–168	–178	–188	–199	–889	–2,042
Provide tax credit for purchase of certain hybrid and fuel cell vehicles .....	–21	–80	–181	–349	–530	–763	–1,903	–3,027
Provide tax credit for energy produced from landfill gas ..	–12	–34	–59	–86	–120	–140	–439	–1,130
Provide tax credit for combined heat and power property	–97	–208	–235	–238	–296	–139	–1,116	–1,091
Provide excise tax exemption (credit) for ethanol <sup>2</sup> .....	—	—	—	—	—	—	—	—
<b>Promote trade:</b>								
Extend and expand Andean trade preferences <sup>5</sup> .....	–130	–192	–213	–226	–58	—	–689	–689
Initiate a new trade preference program for Southeast Europe <sup>5</sup> .....	—	–19	–23	–25	–7	—	–74	–74
Implement free trade agreements with Chile and Singapore <sup>5</sup> .....	—	–21	–86	–109	–131	–155	–502	–1,560
<b>Improve tax administration:</b>								
Implement IRS administrative reforms .....	—	60	49	50	52	54	265	559
<b>Reform unemployment insurance:</b>								
Reform unemployment insurance administrative financing <sup>5</sup> .....	—	–1,002	–1,451	–2,902	–2,982	–4,429	–12,766	–6,924
<b>Expiring Provisions:</b>								
<b>Extend provisions that expired in 2001 for two years:</b>								
Work opportunity tax credit .....	–43	–153	–200	–127	–60	–29	–569	–576
Welfare-to-work tax credit .....	–9	–37	–57	–48	–32	–22	–196	–209
Minimum tax relief for individuals .....	–122	–353	–256	—	—	—	–609	–609

**S-10. Effect of Proposals on Receipts—Continued**

(In millions of dollars)

	2002	2003	2004	2005	2006	2007	Total	
							2003-2007	2003-2012
Exceptions provided under subpart F for certain active financing income.....	-864	-1,502	-630	—	—	—	-2,132	-2,132
Suspension of net income limitation on percentage depletion from marginal oil and gas wells.....	-25	-44	-18	—	—	—	-62	-62
Generalized System of Preferences (GSP) <sup>5</sup> .....	-370	-415	—	—	—	—	-415	-415
Authority to issue qualified zone academy bonds.....	-4	-13	-25	-35	-37	-37	-147	-332
<b>Permanently extend expiring provisions:</b>								
Provisions expiring in 2010:								
Marginal individual income tax rate reductions.....	—	—	—	—	—	—	—	-183,769
Child tax credit <sup>6</sup> .....	—	—	—	—	—	—	—	-31,697
Marriage penalty relief <sup>7</sup> .....	—	—	—	—	—	—	—	-12,976
Education incentives.....	-1	-5	-10	-15	-20	-26	-76	-2,810
Repeal of estate and generation-skipping transfer taxes, and modification of gift taxes.....	178	-550	-1,097	-1,485	-1,987	-2,178	-7,297	-103,659
Modifications of IRAs and pension plans.....	—	—	—	—	—	—	—	-6,490
Other incentives for families and children.....	—	—	—	—	—	—	—	-1,298
Research & Experimentation (R&E) tax credit.....	—	—	-906	-2,949	-4,654	-5,623	-14,132	-51,051
<b>Total budget proposals.....</b>	<b>-64,532</b>	<b>-73,017</b>	<b>-59,130</b>	<b>-27,927</b>	<b>-6,034</b>	<b>-9,433</b>	<b>-175,541</b>	<b>-591,020</b>

<sup>1</sup> Affects both receipts and outlays. Only the receipt effect is shown here. The outlay effect is \$27,000 million for 2002, \$8,000 million for 2003, \$1,500 million for 2004, \$9,500 million for 2003-2007, and \$9,500 million for 2003-2012.

<sup>2</sup> Policy proposal with a receipt effect of zero.

<sup>3</sup> Affects both receipts and outlays. Only the receipt effect is shown here. The outlay effect is \$165 million for 2003, \$449 million for 2004, \$699 million for 2005, \$975 million for 2006, \$1,213 million for 2007, \$3,501 million for 2003-2007, and \$4,155 million for 2003-2012.

<sup>4</sup> Affects both receipts and outlays. Only the receipt effect is shown here. The outlay effect is \$677 million for 2003, \$5,185 million for 2004, \$6,292 million for 2005, \$6,560 million for 2006, \$6,441 million for 2007, \$25,145 million for 2003-2007, and \$59,873 million for 2003-2012.

<sup>5</sup> Net of income offsets.

<sup>6</sup> Affects both receipts and outlays. Only the receipt effect is shown here. The outlay effect is \$8,745 million for 2003-2012.

<sup>7</sup> Affects both receipts and outlays. Only the receipt effect is shown here. The outlay effect is \$1,527 million for 2003-2012.